

FRAMEWORK FOR THE ASSESSMENT OF CONSUMER COMPLIANCE RISK IN BANK HOLDING COMPANIES

December 2003

Consumer compliance supervision of a Large Complex Banking Organization (LCBO) or Large Banking Organization (LBO) includes two components: (A) the consumer compliance risk assessment; and (B) the organization's supervisory plan. These components are discussed below.

A. Consumer Compliance Risk Assessment

The assessment of consumer compliance risk will be carried out in a manner consistent with the supervisory approach used to assess risk in other specialty areas under current BS&R policies.¹ The consumer compliance risk assessment will be performed by consumer compliance examiners whose experience enables them to assess consumer compliance risk across the broad range of a banking organization's activities, and will focus on identifying the type of consumer compliance risk inherent in an organization's business activities. The risk assessment will include a determination as to the level of consumer compliance risk (high, moderate, or low), taking into consideration the internal control and review processes in place to mitigate the inherent risk. Finally, the consumer compliance risk assessment will include a determination as to the direction (increasing, stable, or decreasing) of consumer compliance risk, and will include an analysis of how that risk impacts reputational, operational, legal, or other risks considered in the risk analysis process.²

To the extent possible, the consumer compliance examiner will rely upon work that has been performed by the dedicated supervisory team and/or primary bank regulator, and will then expand on the analysis to focus on consumer compliance risk. For example, the consumer compliance examiner will evaluate the organization's audit function as it relates to consumer compliance. If, after reviewing relevant audit reports, reports obtained from the primary regulator, information from the Central Point of Contact (CPC), and other available information, the consumer compliance examiner identifies areas of significant consumer compliance risk, the consumer compliance examiner will include this factor in discussions with the CPC. The consumer compliance examiner and the CPC will determine, on a case by case basis, whether, and what type of, follow-up activities should be included in the supervisory plan for the organization.

The consumer compliance examiner will discuss the risk assessment findings and conclusions with the CPC, who will include this information in the organization's overall risk assessment. In addition, the CPC and the consumer compliance examiner will coordinate with other regulators, as appropriate, prior to communicating findings to the management of the banking organization. This will help ensure a seamless process in which consistent messages are delivered to LCBO/LBO management, and will facilitate the coordination of activities to be included in the supervisory plan for the organization. Consistent with existing supervision policies for LCBOs and LBOs subject to the System's continuous supervision program, the consumer compliance examiner will update the consumer compliance risk assessment on a

¹ Risk-focused supervision of large complex banking organizations is set forth in SR letters 97-24, 99-15 and 00-13.

²If the LCBO/LBO includes a state member bank, the consumer compliance risk profile for the bank should be used in developing the consumer compliance risk assessment for the LCBO/LBO.

quarterly basis or at any time that new information indicates a change in the organization's risk profile.

The risk assessment will include an evaluation of the adequacy of corporate governance mechanisms at the LCBO/LBO with respect to consumer compliance risk. These mechanisms include board of director and senior management oversight, the structure of the consumer compliance program, policies and procedures, compliance audits/reviews, internal controls, and training. Related management reporting systems will also be evaluated.

The consumer compliance examiner will evaluate the effectiveness of the LCBO/LBO's processes for ensuring compliance with applicable laws and regulations, including but not limited to, the Real Estate Settlement Procedures Act, the Home Mortgage Disclosure Act, the Equal Credit Opportunity Act, the Truth in Lending Act, and the privacy provisions of the Gramm-Leach-Bliley Act.

The consumer compliance examiner will also evaluate the adequacy of the audit program as it relates to consumer compliance and the sufficiency of internal controls, whether the compliance audit function is performed internally or outsourced.³ The consumer compliance examiner will assess the scope of the organization's audit program as it relates to consumer compliance, including the methodologies used to risk-focus the audit approach and the frequency with which audits are conducted. The review will also cover how LCBO/LBO management tracks and follows-up on audit findings to ensure that corrective action is taken. The consumer compliance examiner will assess whether work performed under the audit program adequately enables LCBO/LBO management to reach a valid conclusion regarding compliance with consumer laws and regulations.

B. Supervisory Plan

The CPC develops a supervisory plan for a LCBO/LBO on an annual basis to address the broad range of risks identified in the organization's business activities. The CPC updates the plan on a quarterly basis, or at any time as necessary to reflect a change in the risk assessment. The consumer compliance examiner will participate in this process in the same manner as examiners for other specialty areas. Based on the assessment of consumer compliance risk, the consumer compliance examiner may recommend that the CPC include targeted offsite or onsite consumer compliance activities in the supervisory plan. The supervisory activities will vary depending on the nature and level of an organization's consumer compliance risk. Organizations with a high or moderate level of consumer compliance risk will likely require ongoing or a higher level of supervisory activity than would be necessary for organizations with low levels of consumer compliance risk.

In most cases, LCBO or LBO management will be notified of potential consumer compliance-related weaknesses as part of the ongoing supervision process and will be asked to correct deficiencies noted. The Board's policy not to routinely conduct consumer compliance examinations of nonbank subsidiaries of bank holding companies remains in place. There may, however, be rare instances in which consumer compliance examiners need to conduct an onsite

³ The Risk-Focused Consumer Compliance Supervision Program contains additional information on conducting such reviews and requires consideration of, among other things, the quality, scope and independence of the audit work performed.

examination of a nonbank subsidiary to resolve a significant issue that has the potential for widespread violations or consumer harm. Such situations include, but are not limited to, the failure of an organization to correct an identified problem, or when an organization appears to be incapable of correcting a problem. The decision to include onsite consumer compliance supervisory activities of a nonbank subsidiary in an LCBO or LBO supervisory plan should be made jointly by the consumer compliance examiner, the CPC, and Board staff.